STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
SICA ELECTRICAL & MAINTENANCE CORP.	:	DETERMINATION DTA NO. 813706
for Revision of a Determination or for Refund of Sales and Use Taxes under Articles 28 and 29 of the Tax Law for the period June 1, 1986 through February 28, 1989.	:	

Petitioner, Sica Electrical & Maintenance Corporation, 150-22 Tahoe Street, Ozone Park, New York 11417, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period June 1, 1986 through February 28, 1989.

A hearing was held before Catherine M. Bennett, Administrative Law Judge, at the offices of the Division of Tax Appeals, 500 Federal Street, Troy, New York, on February 14, 1996 at 1:15 P.M., with all briefs to be submitted by July 10, 1996, which date began the six-month period for the issuance of this determination. Petitioner appeared by Lawrence R. Cole & Associates, Inc. (Lawrence R. Cole, C.P.A.). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (James Della Porta, Esq., of counsel).

ISSUES

I. Whether sales tax was erroneously collected by petitioner from its customers for materials used in capital improvement services.

II. Whether the collection of such taxes may apply against petitioner's use tax liability in order to prevent the New York State Department of Taxation and Finance from collection of such sales and use taxes twice on the sale of the same item.

III. Whether the Division of Taxation's computation of petitioner's use tax liability which resulted in the issuance of a Notice and Demand for Payment was supported by the audit workpapers created and submitted in this matter.

IV. Whether the Division of Taxation can properly apply the findings based on a test period audit to a sales tax quarter outside the agreed test period.

FINDINGS OF FACT

The Division of Taxation ("Division") submitted 21 proposed findings of fact. Such proposed findings of fact were incorporated into the findings below to the extent supported by the record. Where necessary, such proposed findings were modified by the Administrative Law Judge, taking into consideration comments submitted by petitioner, and the evidence and testimony comprising the record.

1. During the period March 1, 1986 through February 28, 1989, petitioner performed services as an electrical service contractor providing both capital improvement and repair and maintenance services.

2. In 1989, the Division commenced a sales and use tax field audit of petitioner's records, initially for the period March 1, 1986 through November 30, 1988. Petitioner was advised during the audit that its records available for audit were adequate and sufficient to warrant the utilization of its records for the audit. However, in lieu of utilizing petitioner's entire set of records for such period, petitioner's representative Gloria Sica, executed a consent to a test period audit covering the audit period March 1, 1986 through November 30, 1988. The field audit report revealed that petitioner's sales and purchase records were adequate. Purchases per records were in substantial agreement with purchases reported on petitioner's Federal income tax returns, and gross sales according to petitioner's records were found to be in substantial agreement with sales reported on its Federal income tax returns and sales tax returns. Petitioner maintained a sales tax accrual account and all recorded tax was properly reported.

Ultimately, petitioner was assessed additional tax in the amount of $43,870.39, on the basis of such audit, which was comprised in small part of tax due on the purchase of fixed assets and tax due on certain expense purchases, in addition to tax due on the purchase of materials. With the inclusion of penalty and interest, the Division issued a Statement of Proposed Audit Adjustment dated May 31, 1989, in a total amount of $64,874.27. Petitioner's

representative, Gloria Sica, consented to such amount on behalf of the corporation by her June 8, 1989 signature, and made payment to the Division in the amount of $64,874.27 on June 12, 1989. However, the auditor's log notes reveal that after the case was closed for all practical purposes, the file was returned to the auditor by her group chief to revise the portion of materials purchases that were subject to tax. According to her notes, on July 20, 1989, the Division's auditor telephoned Mrs. Sica to inform her that the audit was on hold and that the consent she signed on June 8, 1989 was revoked.

3. The Division then undertook additional review of the materials purchased by petitioner for use in its capital improvement jobs. The field audit disclosed that transactions petitioner had classified on sales tax returns as taxable and on which it had collected sales tax from its customers were in fact capital improvement jobs. The Division determined that use tax was due on certain material purchases which were incorporated into such capital improvement projects. The Division obtained the amount of purchases of construction materials from petitioner's general ledger for the period June 1, 1986 through November 30, 1988. A later addition for the amount of materials purchased for the period December 1, 1988 through February 28, 1989, was also listed on the work paper. The total of purchases utilized in the Division's computation was $1,528,726.00. This amount was divided into quarterly purchases of construction materials for the sales tax quarters beginning June 1, 1986 through February 28, 1989. The Division applied a factor of 78% to petitioner's purchases per books which were charged to construction jobs as the amount of purchases used in capital improvement jobs. Thus, it was determined that $1,192,406.28 ($1,528,726.00 x 78%), was the amount paid for materials used in capital improvement jobs resulting in tax due on materials of $98,373.54. When added to tax due on expense purchases and fixed asset purchases in the amounts of $1,908.50 and $4,665.06, respectively, the total tax due totalled $104,947.10. Accordingly, a second (and final) statement of proposed audit adjustment dated March 12, 1990, for the period June 1, 1986 through February 28, 1989, asserted tax in the amount of $104,947.10, plus interest of $15,762.17 for a total of $120,709.27. On such statement of proposed audit

adjustment, it was noted that payment of $64,874.27 received on June 12, 1989, would be applied to the amount due as stated above. Gloria Sica on behalf of petitioner consented to have the tax fixed by her signature on March 16, 1990. Preceding Mrs. Sica's signature, is the following inscription on the Statement of Proposed Audit Adjustment:

> "The Tax Law provides that a taxpayer is entitled to have tax due finally and irrevocably fixed by filing a signed consent with the Commissioner of Taxation and Finance. Such consent, subject to review and approval, waives the ninety (90) day period for fixing tax due but does not waive the taxpayer's right to apply for a credit or refund within the time set forth by law. The agreement to and signing of this statement constitutes such a consent. You may consider an approval of this matter final if you are not notified to the contrary within 60 days from the date the signed consent is received by the department."

4. The Division issued a Notice and Demand for Payment of Sales and Use Taxes Due dated March 20, 1990, to Sica Electrical & Maintenance Corporation, in the amount of $104,947.10, plus interest for a total amount due of $120,709.27, for the period June 1, 1986 through February 28, 1989. The former payment of $64,874.27 received on June 12, 1989, was again noted. In addition the Division issued two notices of determination and demands for payment of sales and use taxes due dated March 20, 1990, to the officers of petitioner, Gloria and Michael Sica, in the same amounts, which are not the subject of this hearing. Petitioner paid the remaining tax in accordance with the March 12, 1990 statement of proposed audit adjustment on or before April 25, 1990.

5. An internal memorandum between Division employees appearing as part of the field audit report workpapers provides the following details pertaining to the audit of petitioner:

> "On 6/12/89 we received a consent for tax of $43,870.39, plus penalty and interest of $21,003.88, on the above vendor for the period 3/1/86 - 11/30/88. We received full payment of $64,874.27 and deposited it under S8906120009Q.
>
> Upon final review, it was noted that there was an omission of tax collected by vendor on materials used in C/I jobs and we notified the vendor in writing that we were revoking the consent. Eventually the audit was resolved with the resulting adjusted tax due of $104,947.10. As we have revoked the consent and did not have a waiver to cover the period 3/1/86 - 5/31/86, that period was lost, however our revised audit now covers the period 6/1/86 - 2/28/89.
>
> We issued new assessments . . . and indicated that the previous payment received of $64,874.27 should be applied to it.

Please cancel assessment S890612009Q and transfer the payment received of $64,874.27 to the newest assessments indicated above."

6. Petitioner's representatives, also present at the audit, were consulted about the audit methodology during the audit and reviewed the workpapers which included the 78% allocation before executing the consent to the statement of proposed audit adjustment, and attended meetings at which purchase ratios were discussed. Petitioner's representatives, testifying as to their participation in the audit, did not appear to recall specifically a discussion regarding the 78% ratio in particular, but rather discussed that the issue of ratios had been raised. Petitioner's representative believed that petitioner may have been aware of the 78% figure before Mrs. Sica signed the consent. There is no conclusive proof that the 78% figure was agreed upon between the parties, or to what extent such figure was identified, explained and/or discussed. Neither petitioner nor its representatives presented the auditor with any proof that the purchase ratio figure was less than the 78% used by the Division.

7. The Division provided the testimony of Daniel O'Sullivan, who was responsible for reviewing petitioner's refund claim for the audit period in question. He reviewed the audit workpapers prepared by Maria Stanley, the field auditor in this matter, who retired from State service in April 1994. Mr. O'Sullivan identified the major area of adjustment in petitioner's audit as that pertaining to purchases subject to use tax and incorporated into capital construction projects. Petitioner's representative met with Mr. O'Sullivan on several occasions in regard to his review of the refund application. Although petitioner's representatives did not recall discussing the 78% allocable amount of purchases to capital improvements, petitioner's representatives indicated that Mr. O'Sullivan never refused to consider any of petitioner's records or information submitted to him. Mr. O'Sullivan indicated that if petitioner had established during the refund process that purchases attributable to capital improvement were less than 78%, he would have first reviewed invoices, petitioner's cost accounting system and billings to become certain that proper amounts of tax were paid and remitted in accordance with the Tax Law. If petitioner's representatives had substantiated that the sales attributable to capital

improvements were less than 78%, Mr. O'Sullivan stated he would have then made a favorable adjustment.

Mr. O'Sullivan was asked if he could determine from the file how the figure of 78% was arrived at, or which invoices were disallowed to come up with a percentage equivalent to the 78%. After some discussion, Mr. O'Sullivan admitted that there is not a direct tracing from the 78% calculation through the audit method. In fact, the audit papers do not reference the 78% other than in the application of such percentage to the construction cost materials account. The audit report merely states "78% of vendor's purchases per books charge to construction jobs were assessed, 12% were estimated as used in repair jobs, where vendor charges tax to his customers.[1] Materials were assessed in the amount of $1,192,406.00. Tax due on this is $98,373.54."

8. On March 12, 1992, petitioner filed a refund claim (Claim No. 203530) seeking a refund of $98,373.52 plus interest (the tax due on material purchases only) of the tax paid in accordance with the audit. The refund claim was premised on the following:

> "Vendor was audited and assessed $98,373.54 plus interest for nonpayment of Use tax on materials purchased on completed jobs. The vendor charges sales tax on the retail value of materials used. The Department of Taxation and Finance assessed the vendor on the cost of materials purchased. The State has collected the tax twice - once at the retail level and once at cost and has been
>
> unjustly enriched. SICA paid sales tax during the normal course of business. SICA was also required to pay Use tax on the same items.
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> Use tax is merely complimentary to sales tax and the State cannot collect both. Regulation Section 531.1 states in part that compensating use tax is imposed on every person for use within New York State except to the extent they have been or will be subject to sales tax.
>
> There is also an issue of an invalid test period agreement."

9. On November 4, 1993, the Division issued a refund denial letter to petitioner denying in full its claim for refund of sales tax in the amount of $98,373.52. The denial letter in pertinent part states as follows:

> "This refund claim was denied in light of Section 538.8 p 165-176b where it states the following '... a refund of such erroneous collected tax is allowable to the

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[1]The audit report does not provide additional explanation pertaining to the remaining 10% of purchases.

> purchaser of the non-taxable service or capital improvement. The vendor or contractor is liable for and will be assessed any tax due which he failed to pay on his purchase of tangible personal property used as the ultimate consumer in performing a non-taxable service or capital improvement...'
>
> This determination denying your claim shall, by Law, be final and irrevocable unless you complete the attached Form TA-9.1 and submit same to the Tax Commission for a hearing within 90 days of the date of this letter in accordance with the provisions of Section 1139(B) of the Tax Law."

10. Petitioner filed a request for a Bureau of Conciliation and Mediation Services ("BCMS") conference, in response to the refund denial letter. A conference was held on August 26, 1994 and on February 17, 1995, a BCMS conciliation order was issued sustaining the refund denial. A timely petition was filed on April 5, 1995.

11. Petitioner bought supplies and materials from vendors paying no sales tax at the time of purchase. In using its supplies in capital improvement projects, petitioner itemized sales tax on the invoices it presented to its customers for whom it was performing capital improvement services. Specifically, petitioner collected sales tax on the marked up cost of materials used in its capital improvement jobs. The tax was not itemized as a cost under the materials along with the other costs of the job, but rather listed after the subtotal for material and labor (a below the line charge). By setting forth the invoice in the manner chosen by petitioner, the Division claims that petitioner held itself out as the State's agent in collecting sales tax including the erroneous collections from its customers. Petitioner reported the receipts related to such collections as taxable sales on its sales tax returns and remitted the tax collected to New York State. Petitioner contends it was merely recouping the taxation attributable to the materials at the time the materials were charged to its customer. Petitioner proposes an offset of its use tax liability computed on audit by the taxes it remitted. The Division contends if any of the customers from whom sales tax was collected in regard to capital improvement jobs had timely filed a refund claim, the refunds would have been granted. However, the Division concedes that no vendor connected to petitioner and such practices requested a refund before such requests became time-barred.

12. In correspondence dated March 20, 1990 to the Division, petitioner's representative requested that the penalty be abated for the period June 1, 1986 through February 28, 1989 because "the taxpayer misinterpreted the law." The correspondence further states "the taxpayers charge tax and remit tax on material sales sold separately without labor. They did not pay tax at the source."

13. The Division points out that since reported taxable sales on petitioner's sales tax returns filed for the period in issue include the receipts on capital improvement jobs on which petitioner erroneously collected sales tax, the ratio of reported taxable sales to reported gross sales is not an accurate reflection of the actual taxable to gross sales ratio as suggested by petitioner during the hearing.

14. Petitioner presented the testimony of Mr. Cole and Mr. Hartman, its representatives. Although they participated in the audit, they had vague recollections of what took place during the audit in regard to the calculation of tax due on material purchases. No officer or employee of petitioner appeared or testified at the hearing.

SUMMARY OF THE PARTIES' POSITIONS

15. Petitioner contends that the Division is not entitled to collect sales/use tax twice, i.e., once on the sale of an item, and secondly, as a use tax on the same material, and thus, petitioner should be allowed a credit to offset its use tax, and obtain a refund as a result. Petitioner suggests that the Notice and Demand for Payment of Sales and Use Tax issued to petitioner is invalid since the workpapers in petitioner's audit cannot be followed and do not support such notice. Petitioner additionally argues that the findings based upon a test period agreement cannot be applied to a period outside the agreed audit time frame.

16. The Division argues that sales tax erroneously collected by petitioner from its customers may not apply against its use tax liability. The Division maintains that petitioner erroneously collected sales tax from its customers, though such erroneous collection was properly remitted to the Division. The Division asserts that the 78% ratio employed in the audit was an agreed upon figure between the parties and that petitioner has not adequately established

that its use tax liability is less than that agreed to in accordance with the Statement of Proposed Audit Adjustment. The Division further claims that an estimate of tax due is an insufficient basis to support petitioner's refund claim. The Division further argues that petitioner is precluded from raising issues which were not raised in its refund application, i.e., that the purchases attributable to capital improvements are less than the Division claims were agreed upon during the audit.

CONCLUSIONS OF LAW

A. In general, sales tax is imposed on the receipts from every retail sale of tangible personal property (Tax Law § 1105[a]). The definition of a retail sale excludes the sale of tangible personal property for resale as such (Tax Law § 1101[b][4]). Additionally, Tax Law § 1101(b)(4) provides:

> "[A] sale of any tangible personal property to a contractor, subcontractor or repairman for use or consumption in erecting structures or buildings, or building on, or otherwise adding to, altering, improving, maintaining, servicing or repairing real property, property or land, as the terms real property, property or land are defined in the real property tax law, is deemed to be a retail sale, regardless of whether the tangible personal property is to be resold as such before it is so used or consumed [with exceptions not applicable herein] . . . ."

B. Petitioner first insists on distinguishing its business as primarily that of repairs and maintenance. It claims that its "repairman" status is well established by the fact that the Division included as purchases for capital improvement jobs only 24% of total purchases per general ledger, leaving 76% of the purchases as materials used in repair and maintenance services. The conclusion drawn by petitioner is flawed for a couple of reasons. First, there was no analysis provided of the general ledger accounts for construction materials or materials and supplies, either in the audit workpapers or by petitioner at hearing. Mere postings to such accounts do not validate the category of such expenditures. Furthermore, the unavailability of the auditor and the lack of any notations or workpaper indicating such analysis was performed makes it impossible to conclude that more materials were used in repair and maintenance services than capital improvements. Even if the same could be determined, the sales from capital improvement projects may still well exceed those attributable to repairs and

maintenance, leaving petitioner's conclusion in error. Likewise, petitioner cannot equate the percentage of materials used in a particular type of job to the amount of time it spends performing a certain type of service. Thus, any conclusions petitioner attempts to draw based on categorizing its primary business operations as repairs and maintenance are rejected.

C. The parties agree that petitioner performed some capital improvement work during the period at issue, and thus was liable for tax due on the purchase of materials incorporated into such improvements. This is so because the Tax Law deems petitioner the "retail customer" with regard to such materials. The parties differ however, on their interpretation of whether petitioner erroneously collected sales tax from its customers or merely presented a portion of its expense on its customer's invoice in the form of sales tax.

Whether the collection from petitioner's customers was erroneous, is the first issue in dispute. Petitioner presented its customers with invoices indicating the charges for materials, plus a fee for labor, to reach a subtotal. Thereafter, a tax on materials (computed on the materials being charged to the customer) was added to the subtotal, to result in a final total bill. The sales tax was computed on marked-up materials rather than on the cost of such materials, which would have been the proper base for such computation. The tax was computed after labor and materials were subtotaled, rather than shown as part of the materials charge or above the subtotal as a component item being charged to the customer. Although petitioner argues the placement of the sales tax notation on the invoice is irrelevant, the fact that the sales tax was computed on the marked-up materials and is presented on the invoice as though petitioner was collecting sales tax from its customer, the impression that sales tax is being charged and Sica is collecting the same as an agent for the State rings loud and clear. Since this practice is not in accordance with the sales tax law pertaining to capital improvement projects, the next conclusion that must be drawn is that such collection was an erroneous collection. Regardless of petitioner's intent, it is the manner of presentation and the fact that the billing gave the appearance that petitioner was collecting sales tax from its customer for remittance purposes that forces such a conclusion. This is true, even though petitioner had every right to charge and

recoup from its customers, as a component part of its cost of materials, the sales tax it paid or would have paid on materials purchased for such jobs. Even if erroneously collected or collected in excess of the amount as due (both of which took place herein), the Tax Law requires petitioner in this instance to remit the taxes collected to the Division (Tax Law § 1137[a]), which it did.

Whether petitioner can recover such taxes or receive a credit therefrom is governed by the provisions of Tax Law § 1139, which provides for the refund or credit of sales tax, in pertinent part as follows:

> "(a) In the manner provided in this section the tax commission shall refund or credit any tax, penalty or interest erroneously, illegally or unconstitutionally collected or paid if application therefor shall be filed with the tax commission . . . . (ii) in the case of a tax, penalty or interest paid by the applicant to the tax commission, within three years after the date when such amount was payable under this article . . . . No refund or credit shall be made to any person of tax which he collected from a customer until he shall first establish to the satisfaction of the tax commission, under such regulations as it may prescribe, that he has repaid such tax to the customer. . . ."
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> * * *
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> "(c) A person shall not be entitled to a refund or credit under this section of a tax, interest or penalty which had been determined to be due pursuant to the provisions of section eleven hundred thirty-eight [which governs the determination of sales and use tax when a return is not filed or if a return, when filed, is incorrect or insufficient, and the issuance of a notice of determination] where all opportunities for administrative and judicial review as provided in article forty of this chapter [governing the operation of the Division of Tax Appeals] have been exhausted with respect to such determination. However, a person filing with the commissioner of taxation and finance a signed statement in writing, as provided in subdivision (c) of section eleven hundred thirty-eight, before a determination assessing tax pursuant to subdivision (a) of section eleven hundred thirty-eight is issued, shall, nevertheless, be entitled to apply for a refund or credit pursuant to subdivision (a) and (b) of this section, as long as such application is made within the time limitation set forth in such subdivision (a) or within two years of the date of payment of the amount assessed in accordance with the consent filed, whichever is later, but such application shall be limited to the amount of such payment. . . ." (Emphasis added.)

Tax Law § 1138(c) describes the type of consent represented by Mrs. Sica's signature on the March 12, 1990 Statement of Proposed Audit Adjustment, as follows:

> "A person liable for collection or payment of tax (whether or not a determination assessing a tax pursuant to subdivision (a) of this section has been issued) shall be entitled to have a tax due finally and irrevocably fixed prior to the ninety-day period referred to in subdivision (a) of this section, by filing with the tax

> commission a signed statement in writing, in such form as the tax commission shall prescribe, consenting thereto."

In summary, Tax Law § 1139(a) provides in part that the Division will generally refund or credit tax erroneously collected or paid if an application is filed with the Division in a proper time frame. However, section 1139 also contains a restriction as to when a vendor may claim a refund or credit of sales tax collected from a customer under certain circumstances. It provides that no refund or credit shall be made to any person of tax which such person collected erroneously from a customer until he has first established to the satisfaction of the Division that he repaid such tax to the customer. The Division will upon timely application refund erroneously collected tax to the customer from whom it was collected. However, in this case petitioner would not be entitled to a refund or credit of erroneously collected tax until petitioner first refunds the tax to its customers. The policy is based on the fact that such customers are the parties entitled to such refunds, and will be so granted, if a timely refund application is filed by them. The Division further maintains that the erroneously collected taxes may not be credited against petitioner's use tax liability, computed and paid by petitioner as a result of the audit of its materials purchases.

Petitioner contends that it waited the statutory period before filing a refund claim to ensure that the Division could not be "out of pocket" by claims from both petitioner and its customers. The parties agree that none of petitioner's customers filed refund claims for the "erroneous tax" on capital improvements. Petitioner argues that the Division has unjustly enriched itself by assessing petitioner a use tax in addition to retaining the sales tax petitioner remitted, unless petitioner is allowed to offset its use tax liability by the remittance of the sales tax collected from its customers. In support of its position, petitioner cites Matter of Laux Advertising v. Tully (67 AD2d 1066, 414 NYS2d 53). Laux Advertising involved an advertising agency which prepared brochures and catalogues in which it placed media advertisements for its customers. As part of the process, petitioner prepared "mechanicals", representative facsimiles of an advertisement. Petitioner did not pay sales tax on the materials it had purchased from vendors to prepare the mechanicals, but rather issued exemption certificates

to its vendors. Petitioner would bill its customers for the sales tax on the mechanicals, and if the customer had a direct pay permit, it would pay the sales tax directly to the Division. If the customer did not have such a permit, then petitioner would receive the sales tax and remit it to the Division each quarter. The former State Tax Commission maintained, and the Court supported, its position that petitioner purchased the materials (for the preparation of mechanicals) for its own use in preparing advertisements, not for resale to its customers, and therefore such materials should have been subject to sales tax when purchased by Laux. The Division allowed Laux a credit in the sum of $3000.00 which represented sales tax already collected from its customers and remitted to the Division. Of petitioner's two direct pay customers, who remitted sales tax directly to the Division, one received a refund under a timely application. As to the direct pay customer whose refund was time-barred, petitioner was still held liable for such amount. However, "to prevent the State from recovering that $800 twice", the Court allowed petitioner a credit for that amount, which the direct pay customer erroneously paid to the State (id., 414 NYS2d at 54). The Court in Laux essentially tailored an equitable resolution to a situation that the Tax Law did not and would not now permit (Tax Law §§ 1101, 1105, 1139). Petitioner suggests that to avoid double collection by the Division of the sales tax on the same materials, based on Laux, petitioner should be allowed an offset of its use tax liability, by the amount it remitted to the Division, since none of its customers from which petitioner "erroneously collected" sales tax have filed timely claims for refund.

If Laux was the last word on the issue of offset, even though the result cannot be reconciled with the Tax Law, I would agree with petitioner. However, the Division, in opposition, makes note of Matter of Darien Lake Fun Country, Inc. v. State Tax Commission (68 NY2d 630, 505 NYS2d 58, rearg denied 68 NY2d 808, 506 NYS2d 1038), which I believe must be read in conjunction with this analysis. The Division relies on Darien Lake to reach its conclusion that petitioner should not be able to offset its use tax liability by the sales tax it remitted. In Darien Park, petitioner operated an amusement park which included rides among other attractions. Petitioner sold two types of tickets: one for the use of the park and attractions

other than rides, and another to also make unlimited use of the rides. Petitioner paid no sales tax on its acquisition of the rides which it contended were purchased for "resale" to users of them. It paid tax, however, on the admission tickets. The issue was whether the use of the rides by a ticket holder constituted a resale such that the purchase or lease of the ride equipment by petitioner would be exempt from tax. The Court determined that the use of rides by a ticket holder at the park did not constitute a resale such as to exempt the purchase or lease of ride equipment by the park operator from sales tax. The Court did not decide the question raised by petitioner whether its admission charge to its customers was not taxable, and whether such determination would entitle it to offset against any amount due from it the taxes paid on such charges, since this argument was not raised on the record below. However, the Court, precisely citing Tax Law § 1139(a) stated:

> "More importantly, however, petitioner cannot offset against its obligations as purchasers of the facilities any sums that, if due at all, are due its customers and to obtain refund of which petitioner must show that it 'has repaid such tax to the customer'." (id., 505 NYS2d at 59)

Petitioner argues that the price of admissions was not related to the tax due on equipment. I believe petitioner has misread the case, and thus its key point. The Court of Appeals holding in Darien Lake reaffirms the application of Tax Law § 1139(a) as it relates to an erroneous collection being credited or refunded only to the "customer" entitled to it. To the extent there is no means to reconcile Laux and Darien Lake, the holding in Darien Lake must be followed. Thus, the Division properly determined that petitioner's use tax liability may not be offset by the previously remitted sales tax erroneously collected from its customers, since it has not refunded such funds to its customers.

D. I will turn next to Issues III and IV pertaining to the audit.

When petitioner signed the Statement of Proposed Audit Adjustment, it entitled petitioner to have the tax finally and irrevocably fixed, but did not preclude an application for credit or refund, within the time frame allowed by law (Tax Law § 1139). Such provision allows petitioner the right to raise issues in conjunction with proving its entitlement to a refund, and that may include issues pertaining to audit computation. The Division argues that it need not

establish a rational basis for the audit since petitioner signed the consent to the statement of proposed audit adjustment.

The Division properly obtained petitioner's consent to utilize a test period to conduct its audit, though admittedly, petitioner had adequate books and records. The court decisions have well established that if records are available from which an exact amount of tax can be determined, estimated procedures adopted by the Division become arbitrary and capricious and lack a rational basis (Matter of Chartair, Inc. v. State Tax Commn., 65 Ad2d 44, 411 NYS2d 41). The Division is not shielded from establishing a rational basis for its tax computation merely because petitioner chose to pay the tax to prevent interest from further running, and later file a claim for a refund as allowed by law. Whether a taxpayer's records were, in fact complete and adequate and whether the tax determination based on a test period audit can survive scrutiny must be determined by the administrative process subject to ultimate judicial review (see, Reader's Digest Association, Inc. v. Friedlander, 100 AD2d 871, 474 NYS2d 131, lv denied 64 NY2d 601, 485 NYS2d 1025). Thus, petitioner had every right to raise questions pertaining to the tax computation which is the subject of its claim for refund herein. The fact that each and every issue to be raised with regard to the claim for refund was not defined in its entirety on petitioner's application for refund does not preclude petitioner from raising such issues.

E. Petitioner consented to the use of a test period audit, on the basis of an audit method election form, setting forth the audit period as March 1, 1986 through November 30, 1988. According to the documents contained in the audit file, the first quarter of such audit period was lost due to the Division's revocation of petitioner's first consent. Subsequently, the Division added another sales tax quarter to the end of the audit period. There is no indication that petitioner was advised or otherwise notified of the addition of this quarter, other than by presentation of the Statement of Proposed Audit Adjustment. Petitioner did not execute an additional audit method election covering the additional sales tax quarter. By analogy to the case law which prevents the Division from extending an audit without proper notification to a

taxpayer or a proper request for books and records, any assessment of tax connected to the sales tax quarter December 1, 1988 to February 28, 1989 must be cancelled (Matter of Adamides v. Chu, 134 AD2d 776, 521 NYS2d 826, lv denied 71 NY2d 806, 503 NYS2d 109).

F. Turning to the issue of whether the 78% ratio employed was proper and/or substantiated, the Division argues that petitioner's consent to the audit results is justification for the use of the audit method. Such method presumably would include the computation that calculates tax on 78% of the materials purchased which were charged to construction jobs on petitioner's books. The auditor's testimony, however, indicates that he cannot trace the 78% to any computation made in the audit workpapers. In fact, the only reference to the 78% other than in the calculation itself is in the field audit report attachment sheets indicating the fact that 78% of petitioner's purchases per books charged to construction jobs were assessed. The fact that the 78% amount cannot be explained or linked in any way to petitioner's books and records as a ratio or computation derived therefrom indicates that perhaps the Division sought an external index to apply to this construction materials account. The Division cannot simply ignore a taxpayer's records and use an indirect method of estimating tax due, especially where the books and records are deemed adequate, if the taxpayer's records are readily available and provide an adequate basis on which to determine the amount of tax due (Matter of Christ Cella, Inc. v. State Tax Commn., 102 AD2d 352, 477 NYS2d 858; Matter of Chartair, Inc. v. State Tax Commn., supra). The Tax Appeals Tribunal has well established that the audit record must contain information identifying any external index used by the Division to establish a rational basis for the audit methodology employed (Matter of Fashana, Tax Appeals Tribunal, September 21, 1989). The Tax Appeals Tribunal has also set standards that the Division must at hearing through witnesses or documents be able to respond meaningfully to inquiries regarding the nature of the audit performed. Such information is necessary in order to provide petitioner with an opportunity to meet its burden of proving such methodology unreasonable (Matter of Vincent Basileo, Tax Appeals Tribunal, May 9, 1991; Matter of Fokos Lounge, Tax Appeals Tribunal, March 7, 1991). The Tribunal has rejected the principle that the Division has

an affirmative burden to articulate a rational basis for its assessment where the petitioners fail to make any inquiry into the audit methodology or calculation (Matter of Atlantic & Hudson, Ltd. Partnership, Tax Appeals Tribunal, January 30, 1992). However, where the petitioner has made such inquiry, the Tribunal has held that the Division must at hearing be able to respond as stated above (Matter of William Burns, Tax Appeals Tribunal, April 8, 1994; Matter of Vincent Basileo, supra). Petitioner requested a full explanation of the methodology and computation of tax due. The Division had ample opportunity through repeated questions posed at the hearing to describe the specifics of the computation, it has been unable to provide any explanation pertaining to the 78% ratio employed in the calculation of tax in this matter. Since the Division was unable to provide adequate responses or any explanation pertaining to a primary calculation of the audit, it is concluded that the audit is without rational basis and the taxpayer has sustained its burden of showing that the audit methodology was unreasonable. Accordingly, the use tax imposed upon petitioner for its capital improvement transactions was improperly collected by the Division, not as a matter of law, but as the result of a flawed audit. Since petitioner signed a consent pursuant to Tax Law § 1138(c) and filed its claim for refund within two years (March 12, 1992) of the date of payment (April 25, 1990) of the amount assessed in accordance with the consent filed, petitioner is entitled to a refund in the amount of $98,373.52.

G. The petition of Sica Electrical & Maintenance Corporation is granted in its entirety with a refund due petitioner in the amount of $98,373.52 (see, Conclusions of Law "D", "E" and "F").

DATED: Troy, New York
January 14, 1997

/s/ Catherine M. Bennett
ADMINISTRATIVE LAW JUDGE